

8801

**CANADA'S STAKE IN THE
URUGUAY ROUND AND
THE GATT SYSTEM**

by

Murray G. Smith*

October 1988

* The views expressed are solely those of the author and do not reflect the views of Institute members. / Les vues exprimées ici sont uniquement celles de l'auteur et ne reflètent pas les vues des membres de l'Institut.

TABLE OF CONTENTS

	PAGE
Executive Summary	i
Abrégé	iv
1. Introduction	1
2. The International Economic Context	1
- Global Challenges	
- Shifting Trade Tides	
3. Launching the Round	5
- Objectives of the Major Blocs	
4. The Negotiating Agenda	8
- Tariffs	
- Agriculture	
- Tropical Products	
- Textiles	
- Safeguards	
- "Unfair" Trade	
- Non-Tariff Measures	
- Services	
- Trade-Related Investment Measures	
- Trade-Related Intellectual Property Issues	
5. Strengthening the Trading System	26
- Policy Surveillance	
- Dispute Settlement	
6. Strategic Considerations	28
- Comparison of the Negotiating Agendas	
- Multilateral Negotiations after the FTA	
7. Conclusions	32

Executive Summary

As a medium-sized economy heavily dependent upon trade, Canada has a vital stake in the Uruguay Round of multilateral trade negotiations. In particular Canada has significant interests in improving access to offshore markets. Improved access to offshore markets would help Canadian firms to exploit the opportunities for specialization and economies of scale which would be stimulated by implementation of the Canada-U.S. Free Trade Agreement. Alternatively if Canada does not implement the Free Trade Agreement then Canada will have to rely upon the GATT negotiations to create opportunities to develop a more diversified economy. As well the Canadian economy will need to respond to exchange rate challenges associated with the gradual and possibly irregular reversal of the U.S. trade deficit and other global trade imbalances.

The negotiating agenda for the Uruguay Round is extraordinarily complex and ambitious. The negotiations are attempting to resolve persistent conflicts over agricultural and textiles trade which have defied resolution in previous GATT Rounds. The objectives also include extending GATT rules to services, to certain investment issues and to intellectual property measures. Moreover efforts are being made to strengthen the global trading system.

If Canada does not implement the Free Trade Agreement, Canada will face difficulties in achieving key access objectives in the Uruguay Round. Tariff reductions are not a high priority for the United States, the European Community and Japan in the Round, but Canada faces significant tariff and non-tariff barriers to the export of upgraded resource products and manufactured goods. If

Canada does not implement the Free Trade Agreement then Canada's main preoccupation in the Uruguay Round will be bilateral negotiations with the United States. As in past GATT Rounds, Canada would be forced to neglect negotiations with the European Community, Japan and other countries until the closing stages of the Round.

Although many perceive the GATT negotiations as being a substitute for Free Trade, implementation of the Canada-U.S. Free Trade Agreement would strengthen Canada's negotiating position in the GATT. Having completed the

bilateral negotiation with the United States, Canada could focus its negotiating on efforts on obtaining better access to offshore markets in Europe, Japan and the Pacific Rim.

Even so, Canada will need to continue to make common cause with other smaller developed countries and many developing countries if it wishes to achieve better access for upgraded resource products and better global market prospects for agricultural exports. Canada's support of the Cairns Group is an important vehicle, if real progress in reducing agricultural subsidies and dismantling agricultural trade barriers is to be achieved.

Canada has import sensitivities which will arise in the Uruguay Round negotiations as well. Gradual dismantling of Canadian import barriers in sectors such as textiles and clothing and limiting the use of safeguard measures will facilitate structural adjustment in the Canadian economy. By liberalizing its own import policies, Canada will improve prospects for achievement of its own priorities regarding access to other markets.

Canadian manufacturing and high technology industries have a very significant interest in the liberalization of non-tariff barriers as well. For example, expanded coverage of government purchases under the GATT procurement code could benefit industries such as telecommunications, electrical generation and urban transit equipment which would thereby gain better access to U.S. and offshore markets.

During the Uruguay Round, Canada will need to address the new services, investment and intellectual property issues which proved controversial in the Canada-U.S. negotiations. It appears to be in Canada's interest to broaden to other countries the types of obligations on services and investment performance requirements contained in the Canada-U.S. Free Trade Agreement, but Canadian sensitivities on cultural industries and intellectual property issues could make Canadian participation difficult. Yet, multilateral agreements on these new issues, and related problems pertaining to subsidies and unfair trade, could help

protect Canada against unilateral actions under the trade laws of the United States or the European Community.

As is the case with other confusions about the Free Trade Agreement, Canadians do not understand the potential interaction with the GATT on the issue of subsidies and unfair trade laws. Although the proposed future negotiations on subsidies and trade laws are likely to be difficult, Canada will not be forced to accept silly U.S. arguments.

By signing the Free Trade Agreement, Canada keeps all its rights under the GATT, including the GATT rules regarding subsidies and countervailing duties. The Free Trade Agreement continues to apply GATT subsidy rules but creates a new binational appeal mechanism to interpret the trade laws and a new review mechanism governing changes in the trade laws. Subsidies are also a subject for negotiation in the Uruguay Round. The subsequent future bilateral negotiations on subsidies give Canada an opportunity to improve on the GATT rules as they stand at the end of the Uruguay Round, but if the United States and Canada cannot reach a mutually agreed bilateral subsidies code, the GATT subsidies code will continue to apply.

Strengthening the trading system should be a high priority for Canada. Developing new institutional mechanisms within the GATT to monitor national trade policies will contribute to the opening of world markets and help resolve trade conflicts before they arise. At the same time, Canada, as a relatively small economy should support initiatives to strengthen the dispute settlement procedures of the GATT system with or without Free Trade, Canada has a vital stake in strengthening the multilateral GATT system. A stronger more effective GATT would buttress the rules and dispute settlement processes in the Canada-U.S. Free Trade Agreement, if it is implemented. Without the Free Trade Agreement, the GATT rules and dispute settlement processes would provide Canada with its only defence against aggressive unilateral U.S. actions directed against "unfair" measures by Canadian governments which "burden U.S. commerce". The general dispute settlement mechanism in the Canada-U.S. Free

Trade Agreement provides a model for reform of the GATT, although it is unlikely that all of the innovative features of the bilateral mechanism will be implemented on a multilateral basis.

The forthcoming Montreal Ministerial Meeting in December 1988 will review the Uruguay Round negotiations and indicate the prospects for resolving the key differences in negotiating positions during the Round, but little immediate action can be anticipated. Progress on strengthening the GATT system, however, could be achieved at the Ministerial meeting in Montreal.

It is the middle-sized and smaller economies that have the greatest stake in an open rules based system of international economic relations. Even if Canada increases its negotiating leverage by implementing the Canada-U.S. Free Trade Agreement, Canada will need to participate aggressively in coalitions of like-minded countries — such as the Cairns and de la Paix groups in the Uruguay Round — if Canadian objectives of obtaining improved access to export markets and of fostering a more dynamic domestic economy are to be achieved.

Abrégé

Le Canada étant une puissance économique moyenne fortement tributaire du commerce, l'Uruguay Round de négociations commerciales multilatérales revêt pour lui une importance cruciale. Il est d'un grand intérêt pour le Canada, en particulier, d'améliorer son accès aux marchés d'outre-mer. En effet, cela donnerait aux entreprises canadiennes l'occasion de tirer parti des possibilités de spécialisation et d'économie d'échelle que favoriserait la mise en oeuvre de l'Accord canado-américain de libre-échange. D'un autre côté, si le Canada n'applique pas l'Accord de libre-échange, il lui faudra s'en remettre aux négociations du GATT pour susciter des possibilités de diversifier son économie. De plus, l'économie canadienne devra faire face aux défis en matière de taux de change découlant de la correction progressive, éventuellement par à-coups, du déficit commercial américain et d'autres déséquilibres commerciaux à l'échelle mondiale.

L'ordre du jour des négociations de l'Uruguay Round est extraordinairement complexe et ambitieux. On s'efforce de régler des conflits déjà anciens dans les domaines du commerce des produits agricoles et des textiles. Les séries de négociations précédentes du GATT n'ont pas permis de résoudre ces différends. Les négociations en cours visent également à étendre les règles du GATT au domaine des services, à certaines questions relatives aux investissements et à des mesures de protection de la propriété intellectuelle. On tente en outre de renforcer le système commercial mondial.

Si le Canada ne met pas en oeuvre l'Accord de libre-échange, il éprouvera des difficultés à atteindre dans le cadre de l'Uruguay Round des objectifs décisifs en matière d'accès. La réduction des droits de douane ne constitue pas un objectif prioritaire pour les États-Unis, la Communauté européenne et le Japon dans cette série de négociations, mais le Canada est confronté à d'importantes barrières tarifaires et non tarifaires à l'exportation de produits finis et de produits transformés à base de ressources naturelles. S'il n'applique pas l'Accord

de libre-échange, le Canada devra se préoccuper principalement, dans l'Uruguay Round, de négociations bilatérales avec les États-Unis. Tout comme lors de séries de négociations précédentes du GATT, le Canada se verrait dans l'obligation de reléguer au second plan les négociations avec la Communauté européenne, le Japon et d'autres pays jusqu'aux dernières étapes du Round.

Alors que nombre de personnes voient dans les négociations du GATT une instance remplaçant le libre-échange, la mise en oeuvre de l'Accord canado-américain de libre-échange renforcerait la position de négociation du Canada au sein du GATT. Ayant mené à bien ses négociations bilatérales avec les États-Unis, le Canada pourrait concentrer ses efforts sur l'obtention d'un meilleur accès aux marchés d'Europe, du Japon et des pays du bassin du Pacifique.

Même dans ce contexte, le Canada devra continuer de faire cause commune avec d'autres pays développés de plus petite dimension et avec de nombreux pays en développement afin d'obtenir un meilleur accès pour ses produits transformés à base de ressources naturelles et de meilleures possibilités d'accès aux marchés mondiaux en ce qui concerne les produits agricoles. Le soutien accordé par le Canada au Groupe de Cairns constitue un important moyen de faire en sorte que soient accomplis de réels progrès sur le plan du subventionnement des produits agricoles et du démantèlement des obstacles au commerce de ces produits.

Le Canada a certaines sensibilités aux importations qui feront également l'objet des négociations de l'Uruguay Round. Le démantèlement progressif des obstacles aux importations canadiennes dans des secteurs comme ceux des textiles et du vêtement, et la limitation du recours à des mesures de sauvegarde, faciliteront l'ajustement structurel de l'économie canadienne. En libéralisant ses politiques en matière d'importation, le Canada améliorera ses chances d'atteindre ses propres objectifs prioritaires en ce qui concerne l'accès aux autres marchés.

La libéralisation des barrières non tarifaires présente également une grande importance pour les secteurs industriels canadiens de la transformation et

des techniques de pointe. À titre d'exemple, l'élargissement du champ d'application des marchés publics en vertu du Code des marchés publics du GATT pourrait avoir des retombées bénéfiques pour des secteurs tels que ceux des télécommunications, de la production d'électricité et du matériel de transport en commun dans les villes, qui obtiendraient ainsi un meilleur accès aux marchés des États-Unis et d'outre-mer.

Pendant l'Uruguay Round, le Canada devra aborder les nouvelles questions relatives aux services, aux investissements et à la propriété intellectuelle qui se sont révélées controversées dans ses négociations avec les États-Unis. Il semble qu'il soit dans l'intérêt du Canada d'élargir à d'autres pays les obligations en matière de services et les prescriptions de résultats des investissements figurant dans l'Accord canado-américain de libre-échange, mais les sensibilités du Canada dans le domaine des industries culturelles et à l'égard des questions de propriété intellectuelle pourraient rendre sa participation difficile. Et pourtant, la conclusion d'accords multilatéraux sur ces nouvelles questions, et sur des problèmes connexes liés aux subventions et aux pratiques commerciales déloyales, pourrait aider à protéger le Canada contre des mesures unilatérales prises en vertu des législations commerciales des États-Unis ou de la Communauté européenne.

Tout comme dans le cas de la confusion entourant d'autres dispositions de l'Accord de libre-échange, les Canadiens ne comprennent pas l'éventuelle interaction avec le GATT en ce qui a trait à la question des subventions et des lois concernant les pratiques déloyales. Certes, on peut s'attendre à ce que les futures négociations envisagées sur les subventions et les législations commerciales soient difficiles, mais le Canada ne sera pas tenu d'accepter des arguments insensés de la part des États-Unis.

En signant l'Accord de libre-échange, le Canada conserve tous ses droits en vertu du GATT, y compris les règles du GATT relatives aux subventions et aux droits compensateurs. L'Accord de libre-échange reprend les règles du GATT en matière de subventions, mais il crée un nouveau mécanisme d'appel binational

chargé d'interpréter les législations commerciales, et un nouveau mécanisme d'examen de la modification des législations commerciales. Les subventions font également l'objet de négociations dans le cadre de l'Uruguay Round. Les négociations bilatérales ultérieures sur les subventions donnent au Canada une occasion d'améliorer les règles du GATT qui seront en vigueur à l'issue de l'Uruguay Round. Toutefois, si les États-Unis et le Canada ne parviennent pas à établir d'un commun accord un code bilatéral des subventions, le Code des subventions du GATT continuera de s'appliquer.

Le Canada devrait assigner un rang de priorité élevé au renforcement du système commercial. La mise au point, au sein du GATT, de nouveaux mécanismes institutionnels de surveillance des politiques commerciales nationales contribuera à l'ouverture des marchés mondiaux et à la prévention de conflits commerciaux. Parallèlement à cela, le Canada, étant une économie de dimension relativement modeste, devrait, indépendamment de la question du libre-échange, appuyer les initiatives visant à renforcer les procédures de règlement des différends du système du GATT. Il est d'une importance cruciale pour lui que soit renforcé le système multilatéral du GATT. Le renforcement et l'accroissement de l'efficacité du GATT consolideraient les règles et les processus de règlement des différends de l'Accord canado-américain de libre-échange, s'il est mis en oeuvre. En l'absence de l'Accord de libre-échange, les règles et les processus de règlement des différends du GATT fourniraient au Canada son seul moyen de défense contre des mesures unilatérales agressives de la part des États-Unis visant des mesures "déloyales" prises par des gouvernements canadiens et qui "entravent le commerce américain". Le mécanisme général de règlement des différends prévu dans l'Accord canado-américain de libre-échange fournit au GATT un modèle de la réforme à effectuer, bien qu'il soit improbable que toutes les caractéristiques novatrices du mécanisme bilatéral soient appliquées à l'échelle multilatérale.

La Conférence à l'échelon ministériel qui se tiendra à Montréal en décembre prochain passera en revue les négociations de l'Uruguay Round et donnera une indication des possibilités d'aboutir au règlement des principales

divergences entre les positions prises au cours des négociations. Toutefois, on peut s'attendre à ce que la Conférence n'ait guère d'effets dans l'immédiat. En revanche, des progrès dans le sens du renforcement du système du GATT pourraient être accomplis à l'occasion de la Conférence ministérielle de Montréal.

C'est pour les économies petites et moyennes que revêt la plus grande importance la mise en place d'un système de relations économiques internationales fondé sur la règle de l'ouverture. Même si le Canada accroît son pouvoir de négociation en appliquant son entente commerciale avec les États-Unis, il devra participer énergiquement à des coalitions regroupant des pays partageant la même façon de voir - comme les groupes de Cairns et de la Paix au sein de l'Uruguay Round - afin d'atteindre ses objectifs, à savoir l'amélioration de l'accès aux marchés à l'exportation et la dynamisation de son économie sur le plan intérieur.

Murray Smith

1. Introduction

The Uruguay Round of multilateral negotiations under the General Agreement on Tariffs and Trade (GATT), launched in September 1986 at Punta-del-Este, are seen by some Canadians as an alternative to the Canada-U.S. Free Trade Agreement. Others see the Canada-U.S. Free Trade Agreement and the current GATT negotiations as complements which are pursuing common goals through different means. Whichever view is adopted, and regardless of whether the Canada-U.S. Free Trade Agreement is implemented, Canada has a large stake in the outcome of the Uruguay Round of multilateral negotiations and the evolution of the GATT system.¹

In this paper we note developments in the international economic environment which influence Canada's trading prospects. We then review the main negotiating agenda items in the Uruguay Round, noting issues of particular concern to Canada, examine proposals to reform the trading system, and discuss the strategic implications for Canada.

2. The International Economic Context

Several factors will influence the international environment within which the Canadian economy will be operating in the 1990s and beyond. One set of factors involves longer-term shifts in the currents of global trade and economic activity, including greater rivalry among the industrial countries and the emergence of the newly industrialized economies. A second set of factors involves developments in exchange rates which influence the tidal movements in global trade and services flows, and which will influence competitive opportunities for Canadian industries during the 1990s and into the 21st century.

Global Challenges

In the last forty years, the world has become much more interdependent and the balance of economic power has shifted. Europe and Japan have rebuilt their shattered economies and emerged as economic superpowers. A number of Newly Industrialized Economies (NIEs) are becoming increasingly significant players in the global economy.

Economic interdependence has increased for some reasons which are unrelated to economic policy. A long period of relative peace and security has

fostered the expansion of global commerce. An ongoing revolution in the technology of transportation and communications has reduced, and continues to reduce, economic impediments to international trade in goods and services.

Economic policy among the industrial countries has contributed to increased interdependence as well. The reduction of tariffs and the liberalization of non-tariff barriers, which has occurred under the auspices of the GATT and through regional trading arrangements, has made a significant contribution to the expansion of trade and economic growth in the last forty years. In addition, and despite periodic stresses, strains and occasional crises in the exchange rate system, the International Monetary Fund (IMF) and other international financial institutions have facilitated the maintenance of an open trade and payments system.

The changes wrought during this period can be illustrated by recalling the economic performance of the U.S. and Canadian economies in the 1950s — a period that acquires an increasingly golden hue with the passage of time — and contrast that situation with that which prevails today. In the halcyon days of the 1950s, major U.S. manufacturing industries, such as autos and steel, were largely impervious to offshore competition. These major industrial sectors enjoyed economies of scale in production in the U.S. market, which gave them a competitive advantage relative to producers in third countries. Perhaps more importantly for U.S. multinational firms, their involvement in, and exposure to, the large high-income U.S. market meant that U.S. firms were the first to develop and to introduce new products and techniques.

The situation was somewhat similar on the Canadian side of the border. The Canadian market, although not as large as that of the United States, was substantial and as an exporter of resource products, Canada enjoyed a strong economic position relative to Europe or Japan. Thus, the domestic Canadian market was substantial relative to that of other major industrial economies. For example, in the 1950s Canada was second only to the United States in the size of its domestic market for automobiles. During this period of booming resource

exports, the Canadian tariff played an important role in inducing U.S. manufacturing firms to set up subsidiaries in Canada, rather than exporting from production facilities in the United States. In addition, the British Preferential Tariff system provided an added incentive for investment in manufacturing facilities located in Canada as a way to serve Commonwealth markets.

Today the world is very different. There has been a dramatic increase in global production and competition. Three factors account for much of this increase. First, competition has increased among the advanced high-income countries and there is growing global rivalry among multinational corporations. The integration of the European market through the creation of the European Community (EC) and of the European Free Trade Association (EFTA) and the subsequent linking of these markets through the EFTA-EC bilateral agreements has yielded a single market of 350 million people. Large domestic markets and the higher per capita incomes achieved both in Europe and in Japan, have enabled these economies to offer now many of the potential advantages of economies of scale and innovation to their domestic firms. Thus, European and Japanese industry can now compete much more effectively against U.S. multinational enterprises in the development of new products and new technologies. The growing interpretation of trade and investment by multinational corporations poses particular challenges for Canada which has a heavy preponderance of U.S. subsidiaries.

Second, high rates of economic growth among the group of NIEs have also altered relative competitive positions in international trade. In conjunction with domestic policies that have shifted from an emphasis on import substitution toward a policy of export orientation, countries such as South Korea, Brazil, Taiwan and Spain have become powerful competitors in the basic heavy manufacturing industries. The NIEs are a diverse group, with differences in their domestic policies, in their social and economic structures, and in their external trade and payments regimes, but several of them have emerged as significant international competitors in industries such as automotive production, steel, and shipbuilding, which were traditionally the preserve of the industrialized countries.

Third, a group of countries consisting of developing economies with large populations are shifting from a heavy agricultural orientation toward more industrial production and trade. Economies such as Thailand, the Philippines, Malaysia, and even India and the People's Republic of China are following the path trod by Hong Kong and Taiwan, by pursuing more outward-looking policies and expanding their production and exports in labor-intensive light-manufactured consumer products.

Two fundamental developments have altered the competitive position of the U.S. and Canadian economies. First, the advantages to U.S. producers from economies of scale in production and innovation have declined at the same time that improvements in the technology and infrastructure of transportation and communications have increased global competition. Since Canadian manufacturing is dominated by U.S. multinational enterprises, the decline in the relative position internationally of U.S. firms has important implications for Canada. Second, the comparative advantage of the North American economies is changing as their share of specialized factor endowments, such as highly qualified manpower or modern technologically-advanced physical capital, are declining relative to the positions of the other high-income countries.

In the longer term, the global competitive challenges confronting both the United States and Canada make their respective interests in implementing the Free Trade Agreement more compatible. Each country stands to benefit from the rationalization of U.S. and Canadian multinational enterprises which operate on both sides of the border. Furthermore, much of the adjustment to freer bilateral trade will be intra-industry. Thus, adjustment costs will be minimized, while the opportunities for specialization will be significant. Elimination of tariff and many non-tariff barriers between Canada and the United States under the Canada-U.S. Free Trade Agreement would increase the scope for product specialization and enhance the returns from successful innovation. As a result, the Canadian firms — and U.S. subsidiaries in Canada — will become more competitive with offshore rivals if the Canada-U.S. Free Trade Agreement is implemented. Yet reaping all of the benefits to be derived by Canadian

industries from rationalization in the North American market depends upon obtaining better terms of access to offshore markets. The Uruguay Round is best available vehicle to improve access to such offshore markets.

Shifting Trade Tides

Continuing pressures to reverse global trade imbalances will influence the stance of the major players in the Uruguay Round. The realignment of exchange rates (which has sharply reduced the value of the U.S. dollar in terms of the yen and West German mark since 1985) that is starting the process of reversing global trade imbalances could make it harder to make progress in the Uruguay Round. Protectionism may be waning slowly in the United States, but the legacy of protectionist attitudes are likely to continue to linger. At the same time, Japan and Europe (both with strong currencies) could become less willing to open their markets to competition from foreign agricultural producers and the manufacturing capabilities in developing countries.

Similarly the pattern of Canadian trade is affected by the exchange rate alignment among the major industrial countries. During the 1970s when the U.S. dollar was low, Canada earned all of the trade surplus required to service its international liabilities from offshore trade. During the 1980s with the strong U.S. dollar, Canada obtained all of the necessary trade surplus from trade with the United States and ran a trade deficit with the rest of the world. Although the process could be irregular depending upon the budgetary policies of the next Administration, the United States will be obliged to continue to make progress in reducing its trade deficit. Thus, Canada will need to look to offshore markets for growing export opportunities.

3. Launching the Round

The issues in the Uruguay Round can best be understood with reference to the history of the GATT in the 1980s. In particular, conflicts between the United States and the European Community, which sought support among the developing countries, which erupted at the 1982 GATT ministerial meeting, threatened to undermine the GATT system. Moreover, as the decade unfolded, and as

protectionist pressures grew in the United States with the strong U.S. dollar, the risks that the system would unravel increased. Thus the decision to have a ministerial meeting in Punta-del-Este/Uruguay in September 1986 in an effort to launch another round of multilateral GATT negotiations was not without risk.

The divisions over key issues between the United States and the European Community, which often aligned itself with many developing countries, persisted in the period prior to the Uruguay ministerial meeting. Instead of the major players developing the draft declaration, that task fell to a number of smaller countries, the de la Paix group (which includes Canada, Sweden, Switzerland, Australia, South Korea and Hong Kong and a larger group called the G47); it was these countries that drafted the text which ultimately served to provide the basis for the Punta del Este ministerial declaration. The role of these smaller countries was to broker and bridge the gaps between U.S. and the EC/developing country position on issues such as services.

Although most of those present at the Uruguay ministerial meeting were conscious that failure to develop a joint position launching the Round could have extremely serious consequences for the world trading system, up until the final day of the meeting there was no guarantee that success would be achieved. It took the efforts of the Cairns group of countries, which includes Canada, Australia, New Zealand and nine developing countries, to force agricultural trade issues on the agenda of the Round in a manner that was satisfactory to both the United States and the European Community.

Thus, unlike the Tokyo Round where the agenda and ultimate outcome of the negotiations was determined largely by interaction among the big three — the United States, the European Community and Japan — the Uruguay Round is a much more "multilateral" negotiation. Indeed, the middle powers particularly from the developed countries, although more recently including some of the developing countries, have played a critical role in resolving divisions among the big three and between the developed countries and the developing countries.

Objectives of the Major Blocs

A major objective of the United States is to strengthen the trade rules dealing with subsidies (in particular to limit European subsidies) and to improve the effectiveness of the application of these rules, particularly to sectors such as agriculture. As in past GATT rounds, the United States also seeks improvement in the terms of export market access, and since non-tariff barriers have become more important in constraining the expansion of trade, "negotiations should aim primarily at eliminating such barriers."² The United States attaches a high priority to the "new issues", specifically: the reduction or elimination of barriers to trade in services; the removal of policies which affect direct investment and which indirectly distort trade flows — trade related investment measures, (TRIMs) — and trade related intellectual property issues (TRIPs).

A key to the development of momentum in the multilateral talks is the interests of the other major parties. The European Community's declarations on the Uruguay Round suggest that it has only a limited interest in improvements in export market access. Rather, its most prominent export concern is to obtain more effective means of entry into Japanese markets for manufactured products amid concerns about the Japanese distribution system and the bilateral EC-Japan trade imbalance. The EC supports strengthening trade rules and their application to problems of intellectual property and counterfeit goods, as well as the principle of freer trade in services. In important respects, however, the EC is defensive about its trade policies. While the EC is prepared to negotiate about agricultural trade issues, negotiations that might change key elements of the Common Agricultural Policy (CAP) are likely to be extremely difficult. The EC also takes the view that the negotiations should aim for tariff harmonization by reducing some high tariffs, but that they should not involve across-the-board reductions. The Community is preoccupied with the effort to complete the internal market by 1992 and it remains uncertain how these internal policy developments will influence the EC negotiating position in the Uruguay Round.

Japan's objectives in the Uruguay Round are to obtain greater security of access to markets in general, and to improve access to markets for high-

technology products in particular. Japan also supports efforts to achieve freer trade in services and to develop GATT rules on intellectual property measures. Japan is less willing to liberalize trade in agricultural and primary resource products, because of the political clout of that country's rural sector. Although Japan's approach to the Uruguay Round is cautious and conservative, Japan will be a consistent and constructive participant in the negotiations.

A potentially major obstacle in the Uruguay Round is the conflicting objectives of the industrial countries on the one hand, and the developing countries on the other. Developing countries want liberalized trade in import-sensitive industries, such as clothing and textiles, as well as tighter restrictions on the use of quotas or other safeguard measures in industries such as steel. Most industrial countries (with the partial exception of the EFTA nations), however, are reluctant to accede to these demands. Yet all the industrial countries, including the United States, Japan, Canada, and those in the EC and EFTA, would like the developing countries to accept more obligations under GATT rules, to participate in some reciprocal reduction of trade barriers to goods, and to agree to new trade rules for services, investment, and intellectual property. Yet the developing countries remain attached to the GATT principle of special and differential treatment for themselves. They also resist the extension of GATT rules to trade in services, TRIMs and TRIPs.

4. The Negotiating Agenda

Although the launch of the Round was achieved only with difficulty, the Uruguay Round set itself an extraordinarily ambitious and complex agenda. The negotiations are seeking to resolve long standing and difficult problems in international trade, most notably distortions to agricultural trade, and the exclusion of textiles and clothing from normal GATT rules, as well as resolving the issue of safeguards which had proved to be unresolvable during the Tokyo Round. In addition to continuing and growing problems of old fashioned protectionism in industries such as textiles and steel, the trading system is beset by new conflicts associated with the U.S. mania about unfair trade. Thus subsidies, countervailing duties and other unfair "trade remedy" actions such as

aggressive application of Section 301 of the U.S. Trade Act of 1974 to trade and investment issues have become contentious issues in global trade. In conjunction with these measures that are GATT-legal, there has been a proliferation of "grey-area" measures in the form of voluntary export restraints, technically outside GATT rules, which are used to impose managed trade regimes.

Beyond tackling these difficult issues, the agenda for the Uruguay Round, as noted earlier, seeks to expand the trading rules to deal with issues arising from trade in services, trade related investment measures and trade related aspects of intellectual property regimes. In the absence of progress on these issues, the United States and perhaps also the European Community are prepared to act unilaterally on these issues.

Finally, the negotiations seek to deal with some of the fundamental institutional problems in the world trading system. It is customary to refer to the GATT as one of the pillars of the Bretton Woods system of international economic organizations, but this observation is only partially true. The GATT was intended to be an interim arrangement until the formation of the International Trade Organization (ITO), but the ratification of the ITO failed in the U.S. Congress. Indeed, there is no reference in the text of the GATT to the organization of the GATT Secretariat. The institution of the GATT and the dispute settlement procedures have evolved on the basis of a consensus among the contracting parties. This Round is seeking to address some of the more fundamental issues in the trading system by developing new institutions to monitor trade policies and to strengthen the dispute settlement procedures.

Tariffs

Tariff negotiations have been at the center of the GATT agenda in previous rounds of multilateral negotiations. During the Tokyo Round there was an extensive effort to deal with non-tariff barriers to trade, but significant tariff reductions were an important part of the overall achievement of the negotiations. During this Round, none of the big three have a significant interest in the reduction of tariffs as a means of trade liberalization. The successive

Rounds of GATT negotiations have reduced tariffs on those products of greatest mutual interest to the big three. The developing countries have significant interest in obtaining further reductions of developed country tariffs, but many are reluctant to make even limited tariff concessions to open their own markets.

The lack of significant interest in the reduction of tariffs is a particular problem for Canada. During the Tokyo Round, Canada tried to obtain better access to export markets for processed resource products. Since Europe and Japan impose low or zero tariffs on primary unprocessed resource products and increase their tariffs as the degree of processing of a particular product increases, Canada faces particular barriers to the upgrading of its natural resource products. The tariff formula utilized in the Tokyo Round tended to reduce high tariffs to a greater extent than low tariffs. As a result, little progress was made in reducing the barriers to the export of upgraded resource products from Canada.

In the Uruguay Round, a group of smaller countries, known as the de la Paix group are leading discussions of a proposed method to achieve tariff reductions. Among the members of the de la Paix group are Canada, Switzerland, Sweden, Australia, New Zealand, Hungary, Singapore, Hong Kong, South Korea, Columbia, Uruguay, Pakistan and Zaire. Members of this group are exploring variations of the tariff formula used during the Tokyo Round but modified to encourage or require the elimination or substantial reductions in tariffs of less than 5 per cent. Criteria of this sort would assist greatly in reducing the barriers to exports of upgraded Canadian resource products.

The United States has expressed its strong opposition to a formula approach to tariff reductions, and supports the traditional request and offer approach used in the early days of the GATT. Under the request and offer approach negotiations are conducted on a bilateral basis. In the U.S. view this approach gives the big countries more leverage in the negotiations. At this point the prospect for liberalization of tariffs during the Tokyo Round remains uncertain. In light of the U.S. position, the negotiations might well proceed on a request and offer basis, and not a formula approach as used in the Tokyo Round.

If so, this will have important strategic implications for Canada which we will consider below. Also, Canada will have to identify carefully its priorities for obtaining better access to offshore markets through the tariff negotiations. Specific priorities for expanding exports prospects for processed resource products and selected opportunities to expand exports of secondary manufacturing goods will need to be identified and negotiated on a product by product basis with each of Canada's major trading partners. Canada will need to make common cause with developing countries, if it wishes to make progress on obtaining better access for processed resource products.

Agriculture

As a major exporter of agricultural products Canada has attached a high priority to liberalization of agricultural trade. As a member of the Cairns group, Canada seeks to restrict the proliferation of subsidies to domestic agriculture which are distorting world trade and to obtain liberalization of import barriers in the markets of the European Community, Japan and the United States.

In the Uruguay Round negotiations, the United States has proposed a "zero 2000 option" which would involve the elimination of all trade distorting subsidies and import restrictions by the year 2000. The European Community has indicated a willingness to limit subsidies and to liberalize import restrictions but is extremely hostile to the U.S. proposal for full elimination of both sets of measures. Due to the disproportionate influence of rural constituencies in the governing Liberal Democratic party in Japan, the Japanese government is also opposed to the U.S. proposal, but appears willing to embark on a program of gradual liberalization. Food security concerns are raised by Japan, Korea, and other food importers in the negotiations. Despite some useful progress in the negotiations in Geneva, the agricultural issue remains deeply divisive.

The policy proposal contained in a recent statement by international trade experts entitled **Reforming World Agricultural Trade** is intended to bridge the gaps among these divergent positions.³ This "Ottawa Statement" makes recommendations to guide the agricultural negotiations in the Uruguay Round, as

well as specific proposals for a framework agreement that could be achieved at the mid-term Ministerial review of the GATT negotiations in Montreal in December.

The Ottawa Statement sets out specific guidelines to provide clear direction and impetus to the negotiations and to ensure longer-term reform. It recommends that the Uruguay Round negotiations proceed on a comprehensive basis to obtain agreement on the following:

- ° a program of progressive reductions in the adverse trade effects of agricultural policies;
- ° guidelines for decoupled or trade-neutral farm policies and positive agricultural adjustment programs;
- ° policies to encourage conservation of land and water resources and to improve environmental systems;
- ° stronger and more precise GATT rules, which would be negotiated in parallel with the program of phased reductions in trade-distorting policies;
- ° arrangements to facilitate full participation by developing countries in the negotiations;
- ° new mechanisms for surveillance, consultation, and domestic policy co-ordination; and
- ° the strengthening of GATT dispute-settlement mechanisms.

The statement calls for the completion by the end of 1988 of a framework agreement for proceeding with the negotiations; the agreement must provide clear direction for policy reform and allow for the maximum degree of trade liberalization without prejudging the ultimate outcome.

Several crucial elements must be included in a successful framework agreement. They are:

- ° Identification of the programs that are to be included in negotiations on reducing trade-distorting policies, as well as clarification of a list of programs that clearly would be considered non-distorting and thus could expect relatively few alterations or constraints as a result of future negotiations;
- ° agreements, as specific as possible, on the direction of changes in policies to guide the negotiations on trade-distorting programs and the strengthening of GATT rules;
- ° the role of developing countries;
- ° a surveillance mechanism under GATT to review current policies, monitor changes in policies, and report publicly to member states on the situation;
- ° a dispute settlement process that allows a speedy and non-confrontational settlement of the disputes that are certain to arise during the subsequent negotiation period and beyond; and
- ° short-term measures to be put in place during the remainder of the negotiations and, possibly, during a longer transition period, to deal with severe urgent distortions of international trade, including a freeze on subsidy levels and trade barriers.

This proposed approach to the negotiations will ensure realization of the goal of freer trade in agriculture, while avoiding divisive debate about the zero 2000 option.

Canada as a substantial agricultural exporter stands to benefit from a ceasefire in the agricultural trade wars and a dismantling of agricultural subsidies and import restrictions. Although Canadian income support and supply management programs are less trade-distorting than some of the price support programs of other countries, Canada must be prepared to negotiate specific aspects of these programs if it wishes to achieve the objective of improved market prospects for Canadian agricultural exports.

Tropical Products

Liberalization of tariffs and non-tariff barriers on some of the exports of tropical agricultural products from developing countries has been identified as a high priority in the Uruguay Round. Significant progress could be achieved on products such as beverages and horticultural products which do not compete directly with temperate zone producers by the time of the Ministerial mid-term review in Montreal in December 1988. However, in areas such as grains and oilseeds where serious problems arise in trade among the developed countries, prospects for liberalization remain slight unless the larger agricultural trade issues are resolved, because these tropical products compete directly with temperate zone products.

Although there is a high level commitment to early action on tropical products by the Montreal meeting, the scope of the package is likely to be limited. The European proposal for reduction of barriers on tropical products is narrow in scope, and the Europeans are stressing the need for "burden sharing", by which they mean that other major players should take equivalent steps. The United States is holding back on making a proposal on tropical products, because it is linking progress on this issue to progress on agricultural products. Needless to say, the developing countries are indignant that they are being held hostage to the battle between the United States and the European Community over agricultural trade.

Textiles

Since the early 1960s, exports of textiles and clothing from the "low cost" producers in the third world to the industrialized countries, including Canada, have been subjected to quantitative controls under special arrangements concluded within the GATT framework. From the mid-1970s, the Multifibre Arrangements (MFA) has provided the cover for these restrictive controls. Most industrialized countries, including Canada, also impose their highest tariffs on imports of textiles and clothing from all sources. The cumulative impact of Canadian tariffs and the MFA quotas results in high trade barriers against apparel exports of developing countries.

The ministerial declaration for the Uruguay Round proposes the objective of formulating "modalities that would permit the eventual integration of this sector in the GATT on the basis of strengthened GATT rules and disciplines".⁴ Unraveling the complicated structure of tariff and non-tariff protection in the textiles and apparel sectors is likely to prove at least as difficult a task as resolving agricultural trade issues. Textiles and apparel represent one area of international trade where international barriers have been rising, not declining. There have been marginal declines in apparel tariffs to average levels of 22 1/2 per cent in the the United States and 14 per cent in the European Community and Japan, but quota restrictions under the Multifibre Arrangement have been extended both in terms of product coverage and the number of low-cost countries involved. Cline estimates that since the mid 1960s the combined tariff and non-tariff protection for U.S. apparel imports has nearly doubled, to a combined 56 per cent tariff-equivalent protection. On a global basis, quotas under the MFA cover approximately 60 per cent of textiles trade and 65 per cent of apparel trade.⁵ The remaining trade occurs primarily among the industrial countries which retain high tariffs, but which do not, as a rule, apply quotas among themselves.

The textile and clothing sectors are among the most protected industries in the Canadian economy. Much of the protection is now focussed on the apparel industry. Since the late 1970s, the bilateral quota restrictions that Canada has

concluded with low-cost suppliers under the Multifibre Arrangement are heavily concentrated in the apparel sector, and few now apply to textiles. Canadian textiles and apparel tariffs are in the 20-25 per cent range; they are higher than in the United States and probably the highest among the larger industrial countries. The Canadian apparel industry depends to a substantial degree on imported fabrics and, in some cases, can obtain these fabrics duty-free through specific tariff orders granted by the Department of Finance. Moreover, Canada has some selective duty remission programs which provide apparel manufacturers with additional relief from Canadian textile tariffs; these, understandably, become highly controversial with the United States in the context of the bilateral Canada-U.S. Free Trade Agreement because they are prohibited under the Agreement, except for a specified time period. The Canadian government has indicated that it plans to lower the MFN tariffs on imported fabrics used by apparel manufacturers in cases where those tariffs are significantly above U.S. tariffs levels.

The Uruguay Round provides an opportunity to limit the spread of protectionism and to start liberalization of one of the most protected sectors in international commerce — textiles and clothing. However, although Canada may be receptive to liberalization of trade in textiles, its garment manufacturers are likely to resist efforts to liberalize apparel trade and to bring the MFA under stricter disciplines. Nevertheless, the Canadian economy as a whole, would benefit if the Uruguay Round were to agree to a program of retarification which would gradually replace and eliminate the MFA quota restrictions and then start the process of tariff reductions for these highly protected industries. Alternatively, the industrial countries could enter into a commitment to phase out the MFA by a set date. Such an approach would encounter domestic resistance in Canada as well as in the United States and the European Community; but if adopted by the major industrial countries it would provide a powerful inducement for some of the developing countries to participate more fully in the trading system.

Safeguards

Safeguard import measures under Article XIX of the GATT have often been a vehicle for giving additional protection to producers in the developed countries. Such measures were originally intended to respond to surges in imports that injured domestic producers by offering temporary relief in the form of delay or suspension of tariff reductions which have been negotiated in a trade agreement, or by imposing quantitative controls temporarily. However, in recent years, the safeguard provisions of GATT have been used more and more extensively, especially by the United States and the European Community to restrict import competition on a longer term basis and to enforce managed trade regimes in sectors such as footwear, steel, automobiles and other products. And the disciplines of the GATT rules over the use of Article XIX safeguards measures have even more often been evaded by the use of "grey-area" restrictive measures with similar effects.

The use of safeguard provisions was a major issue in the Tokyo Round of multilateral negotiations, but those issues proved not to be resolvable. One obstacle was the European Community effort to legitimize the use of "selective" safeguards directed against particular countries; another was pressure by the developing countries to create stricter disciplines on the use of safeguard measures. The issues surrounding the use of safeguards have become even more difficult since the conclusion of the Tokyo Round. Not only has there been broader application of explicit safeguard measures under Article XIX of the GATT, but there has been a proliferation of "grey-area" measures such as voluntary export restraints which are technically outside of the GATT.

Negotiations on safeguards face a dilemma. If more stringent criteria are introduced which limit the application of safeguard measures under Article XIX, then such stringent criteria for Article XIX safeguards measures could lead to a further proliferation of grey-area measures which are beyond GATT rules and disciplines.

Some argue that it would be counterproductive to negotiate about grey-area measures such as voluntary export restraint arrangements currently outside GATT rules, because such negotiations could have the effect of codifying these practices and legitimizing them. If the drift toward managed trade is to be reversed, however, it will be important to bring the widest possible range of protectionist measures under GATT rules. Perhaps the most productive approach would be to stress the degressivity or phasing out of these measures, to establish clear time limits for their elimination and to develop new multilateral surveillance mechanisms to monitor the use of safeguards.

"Unfair" Trade

Some of the managed trade regimes of the 1980s were imposed under the guise of attacks on "unfair" trade practices. The U.S. countervailing duty case in 1986 with respect to Canadian softwood lumber stands out as a notable example. The unfair trade issues are being dealt within the GATT in negotiations in the group on **Subsidies and Countervailing Duties** as well as in review of the antidumping code in the group on **MTN Agreements and Arrangements**.

Subsidies issues have become among some of the more divisive in international trade. Apart from Canada's experience with softwood lumber, the issue of subsidies has been a source of recent and serious conflict between the United States and the European Community over the case of Airbus Industries. The U.S. view is that massive European subsidies are giving Airbus an unfair advantage in international commerce. The Europeans counter that some of the subsidies in Europe have resulted from unforeseen realignments in exchange rates and, moreover, that U.S. civil aircraft producers receive substantial benefits from government funding for research and development as well as preferential procurement contracts from U.S. military programs.

It would be in Canada's interest to promote multilateral disciplines on the use of industry specific subsidies which are intended to create monopoly positions in international trade, as may be the case in civil aircraft. Even if this does not prove feasible in the GATT, progress in the Uruguay Round in

developing agreed standards and definitions of subsidies, and techniques for the measurement of subsidies, could significantly benefit Canada in bilateral negotiations with the United States aimed at developing common rules on these issues under the Free Trade Agreement.

Negotiations on other unfair trade issues are proceeding in the GATT as well. The U.S. position on antidumping systems, for example, is heavily influenced by recent proposals in the U.S. Congress to strengthen the enforcement of U.S. trade laws. Whereas in the Kennedy Round the United States sought to limit Canada's administrative discretion in the application and enforcement of its antidumping laws, today the United States is preoccupied with an enforcement mentality which is trying to plug holes in the dyke of the U.S. unfair trade laws. Thus sanctions against "recidivist" dumping rank high on U.S. negotiating priorities. By "recidivist" dumping United States negotiators are referring to "repeat offenders". Thus, they are seeking to impute criminal behaviour to firms engaged in international price competition.

If one believes that international competition is to be encouraged and not hindered, then some of the proposals for amendment of the GATT antidumping code and other rules governing unfair trade practices are likely to be counterproductive to the objectives of an open multilateral trading system. Instead, these negotiations should aim at making the administration of trade laws more transparent and reducing their protectionist effects.

Non-Tariff Measures

Some non-tariff barrier issues are discussed in a separate working group on **Non-Tariff Measures**; others in individual sectoral working groups such as **Natural Resource Products**; and still others in the working group on **MTN Agreements and Arrangements**.

Procurement preferences are among one of the more significant non-tariff barriers to trade which are addressed only to a limited extent by the Tokyo Round code on government procurement. Elimination of internal procurement

preferences is a significant element in the proposed efforts by the European Community to complete its internal market by 1992. If the Community is making good progress in these internal efforts, it may be reluctant to open European government procurement markets to international competition. But, if European efforts are flagging, progress in these issues in the GATT might help resolve internal EC differences.

Procurement issues have been a source of conflict between the United States and Japan, as well. An enlargement of commitments under the GATT procurement code could help to resolve some of these U.S.-Japan differences.

For Canada, an enlargement of the coverage of the GATT procurement code could offer significant benefits. The provisions of the Canada-U.S. FTA with respect to government procurement are limited to entities covered under the GATT procurement code. The Canada-U.S. FTA simply expands the purchases covered by imposing a lower threshold with respect to contract awards and also establishes a new mechanism for review of contract procedures and awards. In the context of the Free Trade Agreement, Canada would be a significant beneficiary if the multilateral GATT procurement code were extended to cover sectors such as telecommunications equipment, heavy electrical generation equipment and urban transit equipment. Broadening the coverage of the procurement code would open up markets simultaneously in the United States, the European Community, and the EFTA countries.

Services

The GATT negotiations on services are still at an early stage. A number of countries have tabled proposals for a framework agreement on services and there is some agreement of some basic concepts, most notably elaboration of the concept of "national treatment" which is embodied in the GATT rules for merchandise trade. A national treatment commitment should not be difficult. Most industrial countries are signatories to bilateral commercial treaties which contain national treatment obligations for investment and some services.

It is also proposed that a framework agreement should include the right of establishment and deal with the potential predatory practices of state monopolies. But serious questions remain about the sectoral coverage of such a framework agreement and the nature of the institutional mechanisms which will govern services trade.

The U.S. proposal in Geneva involves the conclusion of a framework agreement analogous to that contained in the Canada-U.S. Free Trade Agreement and proposes a three step process to liberalize trade in services. The first step would be agreement on the framework rules and provisions; the second step would be agreement on the specific services activities to be covered; and the third phase would be the negotiations of rollback measures (reservations to, or derogations from, the initial agreement) which impede trade in services or deviate from national treatment. Thus, the United States seeks to avoid some of the grandfathering of restrictions on services trade and departures from national treatment which are permitted in chapters 14 and 16 of the Canada-U.S. Free Trade Agreement.

During the 1982 GATT ministerial meeting, the United States attempted to bring services into the GATT in order to apply its "unfair" trade laws in the services sector. It is noteworthy that the U.S. services proposal in the Uruguay Round (and also the relevant provisions of the Canada-U.S. FTA) does not make provision for the application of countervailing duty, antidumping duty or other specific actions in the services sector. Of course, it is possible under U.S. law to pursue section 301 actions against foreign practices which burden U.S. commerce. Furthermore, the recent legislative changes to section 301 increase the likelihood of retaliatory action. Thus, unilateral U.S. actions can be taken now against Canadian policies and in the absence of either a multilateral agreement on trade in services or the services chapter and dispute settlement mechanisms in the Canada-U.S. Free Trade Agreement, there are no international constraints on U.S. retaliatory powers.

The U.S. proposal in the Uruguay Round refers to the need for an effective dispute settlement mechanism, although it is not very explicit on this point. The advantage of a rules based system of dispute settlement, as discussed below, is that it provides a more secure and predictable regime for the private sector. It has the additional virtue that an international dispute settlement mechanism (whether in the FTA or the GATT) provides significant protection against unilateral U.S. trade actions, because section 301 provisions require resort to an international dispute settlement mechanism, when such a mechanism is contained in an international agreement.

The E.C. approach in Geneva to trade in services seems to parallel the internal operations of the Community. Instead of a clear set of international obligations covering specific services activities, the Community seeks to have a supervisory committee which would monitor national policies and regulatory measures affecting trade in services. Services regulations would be notified to this monitoring body and their appropriateness judged in light of the norms established in a GATT services agreement. Thus, the services agreement would create a permanent supervisory body which would review individual national services policies and regulations in detail. The E.C. proposals also suggest that an unspecified, but large number of specific sectoral services agreements may be necessary in order to give effect to the overall framework arrangement.

Developing countries, led by Brazil and India, resisted strongly the U.S. proposals to include services in the GATT at 1982 Ministerial meeting and during the subsequent efforts to launch the Uruguay Round. Subsequent analysis (Bhagwati, 1986) and debate has led to some moderation in the positions of at least some developing countries. Developing countries are no longer taking a hard line as a bloc opposed to the negotiations on services. Argentina, for example, has presented a paper which makes suggestions for a services agreement suggesting that it would be prepared to participate if progress could be made on other issues such as agriculture. Nonetheless developing countries are wary of a possible services agreement and uncertain about how they might participate in the agreement.

Subject to the specific provisions of the arrangements which might be negotiated on services in the Uruguay Round, it would be in Canada's interests to broaden the number of countries which have contractual obligations with respect to controls on trade in services or related investment issues. Several caveats should be kept in mind. First, it would be important to extend the exclusion of cultural industries which was obtained in the Canada-U.S. Free Trade Agreement to any multilateral arrangement. Failure to exclude the cultural industries in the multilateral services agreement could make participation unattractive to many Canadians. Second, it is important to avoid a supranational mechanism which could impose additional delays on decision making as well as raising concerns about national sovereignty. Third, it may be difficult to balance the rights and obligations of a large number of countries under a general services agreement of the sort proposed by the United States. Thus, specific sectoral agreements may well be necessary to give effect to the overall framework agreement. Fourth, the Uruguay Round negotiations on services have not yet focussed on the specific form of the dispute-settlement mechanisms which might be adopted as part of a new services agreement under the GATT framework. Whatever the substantive provisions of new arrangements for trade in services, it is in Canada's interest to adopt a dispute-settlement mechanism for services analogous to that in the general dispute-settlement mechanism proposed in the Canada-U.S. Free Trade Agreement, in order to avoid potential unilateral measures directed against Canadian service industries or government policies.

In an increasingly interdependent world, barriers to trade in services can be barriers to trade in goods and vice versa. Canadian industries would benefit from a multilateral services agreement as exporters of services, as importers of services, as exporters of goods and as producers of complex bundles of goods and services. Services issues are almost unavoidable in a global economy governed by nation states, but the litmus test for Canada is whether a multilateral services agreement does in fact create a more transparent, a more open, and a more predictable international regime for services transactions.

Trade-Related Investment Measures

There is a separate negotiating group dealing with trade related investment measures (TRIMs). This group is attempting to deal with various kinds of performance requirements which governments obtain from firms as a condition for investing in their countries. The undertaking regarding performance obtained by the former Foreign Investment Review Agency (FIRA) in Canada was the subject of a GATT dispute settlement process in the early 1980s. The GATT panel report, which was accepted by Canada, found that the undertakings extracted from foreign firms to reduce import sourcing were contrary to the GATT, but that undertakings pertaining to increased exports were not covered explicitly by GATT rules. The developed countries are seeking in the Uruguay to amend the GATT rules to permit a much narrower range of performance requirements that may be extracted from foreign investors.

Because Canada has agreed in the GATT to forego import performance requirements in the FIRA case, and in light of the commitment to cease obtaining export performance requirements in the Canada-U.S. Free Trade Agreement, it would seem to be in Canada's interest to support the adoption of analogous rules on a multilateral basis within GATT. Indeed, Canada as an exporter of processed natural resource products will benefit from improved discipline over the policies and practices of developing countries aimed at extracting performance requirements as a condition of foreign investment in their resource sectors. Developing countries, however, are likely to resist an extension of the GATT agreement to deal with these trade-related investment measures or performance requirements. Thus, these negotiations could yield a conditional MFN code to which only the industrial countries and a few developing countries may choose to accede. Even on this more limited basis, Canadian participation appears desirable, particularly if participation promotes Canadian objectives in other sectors such as improved access for its exports of processed resource products and manufactured goods.

Trade-Related Intellectual Property Issues

The group on **Trade-Related Intellectual Property Issues (TRIPs)** is negotiating one of the most controversial set of issues in the Uruguay Round. These issues overlap those surrounding trade in services, investment and high technology procurement. With the globalization of production and trade in many industries, including the high technology industries, the United States and most other developed countries is attaching a high priority to obtaining greater protection of intellectual property rights, and embodying this protection in new GATT rules. Many developing countries, however, stress the importance of access to technology and are much less concerned about protection of incentives to innovate. A publication prepared for developing countries on the Uruguay Round by UNCTAD contains the following observation:

"From the point of view of developing countries an important concern is for a clear recognition of their legitimate rights to take action to prevent the abuse of intellectual property (e.g. market control, unjustified high rent, etc), as well as to develop their own knowledge intensive industries, without running the risk of trade reprisal... Vital technological and trading interests of our countries are involved in the TRIPS negotiations and the search for solutions which satisfy all parties is likely to be difficult, and may be linked to developments in the other negotiating groups.⁶

Canada has a major interest in the TRIPS negotiations as a major trading country, and as a major importer of technology. Canadian producer interests extend both to trade in counterfeit goods — where there is an abuse of trademarks — as well as to more difficult issues of establishing appropriate standards of patent and copyright protection in the laws of Canada and its trading partners. A further issue is the role of GATT in this area. Some of the more aggressive supporters of negotiations on intellectual property in the United States favour the promulgation within the GATT of standards of intellectual property protection. Others, including the Atlantic Council in the United States, suggest that the GATT may be most effective in dealing with the problem of counterfeit goods and helping in the enforcement of intellectual property regimes which effect international trade; but they argue that the appropriate

standards should be developed by other organizations such as the World Intellectual Property Organization (WIPO), not by the GATT.⁷

In the negotiations of TRIPS, Canada may find itself closer to the position of developing countries. Certainly, drug manufacturers in the United States and continental Europe regard Canada's compulsory patent licensing regime and the performance requirements recently introduced with respect to research and development by pharmaceutical companies, to be an abuse of their intellectual property rights and to be a distortion of international trade.

The tendency towards unilateral actions by the United States and the European Community directed against foreign countries which do not provide 'sufficient' protection of intellectual property rights may lead Canada to be more forthcoming in the GATT negotiations on this issue than Canada was prepared to be in the bilateral Free Trade negotiations with the United States. The 1988 omnibus U.S. trade legislation amends Section 337 of Tariff Act of 1930 to make the provision more onerous, and more accessible, U.S. penalties against infringement of intellectual property rights. Thus, Canadians may need to recalculate the relative benefits of Canada's pharmaceutical licensing regime as compared with the potential costs of retaliation against Canadian exports. Participation in a GATT agreement on intellectual property may involve some additional international obligations to protect intellectual property, but could offer significant protection against such unilateral actions.

5. Strengthening the Trading System

The stresses in the global trading system in the 1980s have made more visible some of the weaknesses in its institutional elements, as well as in the trade rules. Proposals to reform the trading system have been made both before and during the Uruguay Round. Some of these proposals could come to fruition by the time of the Ministerial mid-term review in Montreal in December 1988.

The reform proposals involve two separate but complementary elements. The first involves the development within the GATT of new mechanisms for the

surveillance of national trade policies. The second element involves a strengthening of the GATT procedures for the settlement of trade disputes.

Policy Surveillance

The Uruguay Round has already created a new surveillance mechanism to monitor compliance with the standstill and rollback provisions contained in the Punta-del-Este declaration. Negotiations are preceeding in the group called **Functioning of the GATT System** to develop this type of surveillance mechanism on a permanent basis.

The rationale for surveillance bodies or mechanisms was set out in the 1985 report of the Leutwiler group of wisemen.⁸ Since the GATT system functions in part on the basis of international pressure, the publication of regular studies documenting the protectionist effects of trade policies, combined with regular ministerial meetings to review national trade policies, would make protectionism more visible and transparent and help mobilize pressures for trade liberalization.⁹

Dispute Settlement

International scholars describe regimes for resolving trade disputes as being characterized by either of two extremes. One extreme is a power-based system where a dispute is resolved by ad hoc bargaining between the parties. Often larger countries prefer this type of regime because they can exert greater leverage over smaller countries and trading partners. At the other extreme is a rules-based system, where disputes are resolved by reference to specific contractual obligations or norms, and are subject to adjudication by impartial judges or arbitrators.¹⁰

The GATT dispute settlement mechanism has developed some of the features of a rules-based system in the form of references to independent panels to investigate whether GATT rules have been breached. However, the GATT dispute settlement mechanism remains fundamentally a consensus system. This makes it possible, on occasion, for a large country such as the United States or

the European Community to stonewall the creation of a panel to investigate a trade dispute, or to block the acceptance of a GATT panel report when it is presented, if the outcome is unfavourable to its interests.

The general dispute settlement mechanism in the Canada-U.S. Free Trade Agreement conforms more closely to a rules-based regime. Apart from the reference to binding arbitration when both parties agree, either party can request a panel and the process is then automatically initiated. Furthermore, there are strict procedures and timetables for panel deliberations and for decisions on panel reports by the Canada-U.S. Trade Commission.¹¹

Proposals for the reform of the GATT dispute settlement mechanism would involve the adoption of some of the features of the Canada-U.S. Free Trade Agreement. Progress is being made on developing stricter timetables and improving the procedures for the operation of panels; but the major players, most notably the European Community, are resisting the concept of automatic initiation and acceptance of panel investigations.

Canada's interest, as a highly trade dependent economy which is smaller than the economies of the European Community, the United States or Japan, clearly lies in strengthening the GATT dispute settlement procedures. In particular it is in Canada's interest to support a rules-based system which would provide for the automatic initiation of panel investigations, and for the mandatory adoption of panel reports if they are not accepted by the parties to a dispute within a set period of time.

6. Strategic Considerations

It is useful to compare and contrast the agenda of the bilateral Canada-U.S. negotiations and the Uruguay Round of multilateral negotiations. A discussion of the strategic considerations for Canada in the Uruguay Round in light of whether or not Canada proceeds with implementation of the Canada-U.S. Free Trade Agreement follows.

Comparison of the Negotiating Agendas

Although the negotiating agenda in the Uruguay Round covers many of the same issues as the Canada-U.S. Free Trade negotiations, different negotiating issues are likely to have different fates. For example, tariff elimination in the industrial sectors was a key goal of the bilateral negotiations. The same objective, however, is unlikely to be realized in the multilateral talks because of the negotiating positions of Europe, the United States, and the developing countries.

Quite the reverse is true with agriculture. Important elements of agricultural trade (such as quotas necessary to maintain marketing boards) were exempted from the bilateral negotiations, at least in part because many of the difficulties of Canadian and U.S. agriculture stem from the policies of the EC and Japan. Canada attaches a high priority to the liberalization of agricultural trade in the Uruguay Round, and thus must be prepared to negotiate on import barriers and subsidy practices in the GATT.

At the same time, it is important to recognize that some of the more controversial aspects of the Canada-U.S. Free Trade Agreement are issues that are high on the agenda for the Uruguay Round. In particular, Canadians who are concerned about services and investment provisions of the Canada-U.S. Free Trade Agreement should recognize that Canada's willingness to participate in multilateral agreements on services, investment and intellectual property will influence the prospects for Canada to resolve agricultural trade problems and to obtain better access to offshore markets for upgraded resource and manufactured products.

The major GATT trading partners apparently share the common objective of strengthening GATT rules and dispute-settlement processes, but Canada should press other countries to give practical effect to these general principles in the Uruguay Round. In this respect, the Canada-U.S. Free Trade Agreement could offer some useful models and precedents, although the specific Canada-U.S. mechanisms are likely to remain unique to the bilateral relationship.

Multilateral Negotiations after the FTA

The crucial difference between a free trade area and a customs union is that in a free trade area each member maintains control over commercial policy for, and trade negotiations with, third countries. From the point of view of each member country, the preferential access created by the regional trade arrangements has the character of a public good. It is the external trade barriers of one country that creates the preference for suppliers in the other country relative to third countries.

If implemented, the Canada-U.S. Free Trade Agreement can be expected to shift the focus of multilateral tariff negotiations, promote restructuring of the domestic industry, and improve Canadian industry's capability to meet third-country competition. In general, a free trade area partner has an incentive to negotiate reductions in its external trade barriers in the multilateral forum in order to obtain improved access to third-country markets; whereas in a customs union the maintenance of external barriers becomes the *raison d'être* of the organization. Thus, the preferences created by a free trade area are more likely to be reduced over time through multilateral negotiations than is the case with the customs union.

To illustrate this point, let us consider the following example. Canada's post Tokyo Round tariff on machinery is 9.2 percent. In the absence of the Free Trade Agreement, under the GATT principal supplier rule Canada still would negotiate most machinery tariffs bilaterally with the United States because the United States is the principal supplier of the products. With phased tariff elimination between Canada and the United States under the Free Trade Agreement, U.S. machinery suppliers would have an advantage in the Canadian market relative to producers in third countries such as Japan or West Germany. Depending upon the type of machinery involved, either Japan or the EC would become the principal supplier after the Free Trade Agreement came into effect. Subsequently, in GATT tariff negotiations, Canada could offer to lower its machinery tariff in order to obtain reciprocal reductions in Japanese or EC trade barriers of interest to Canada.

In contrast, a common market with elaborate supranational institutions such as the European Community is less likely to be outward looking in its orientation. Indeed, the drive to complete the internal market of the European Community by 1992 will have an important influence on the Uruguay Round. It is too soon, however, to judge the precise nature of this interaction. The Community may see multilateral progress in liberalizing government procurement and services trade as a way to achieve its internal objectives. Alternatively, however, Europe may seek to open its internal market while maintaining or increasing protection against third country competition.

Canada (and also the United States) recognize that the members of a free trade area have a continuing interest in the international trade rules which provide the framework for managing trade relations and trade disputes. Each member continues to have separate trade relations with third countries, and important elements of the multilateral rules will continue to govern their trade.

Multilateral Negotiations Without the FTA

If Canada does not implement the Free Trade Agreement, Canada will face difficulties in achieving key access objectives in the Uruguay Round. Tariff reductions are not a high priority for the United States, the European Community and Japan in the Round, but Canada faces significant tariff and non-tariff barriers to the export of upgraded resource products and manufactured goods. If Canada does not implement the Free Trade Agreement then Canada's main preoccupation in the Uruguay Round will be bilateral negotiations with the United States. It would be necessary to start over in difficult tariff negotiations with the United States. As in past GATT Rounds, Canada would be forced to neglect negotiations with the European Community, Japan and other countries until the closing stages of the Round. Canada's limited leverage in obtaining better access to offshore markets would be eroded greatly.

In the Uruguay Round, Canada will need to address the services, investment and intellectual property issues which proved controversial in the Canada-U.S. negotiations, since these issues are high priorities for the big three.

Canadian sensitivities on cultural industries and intellectual property issues may make Canadian participation difficult. Yet, multilateral agreements on these new issues, and related problems pertaining to subsidies and unfair trade, could help protect Canada against unilateral actions under the trade laws of the United States or the European Community.

7. Conclusions

The Uruguay Round is the most complex and protracted set of multilateral negotiations ever held under GATT auspices. Old problems such as agricultural trade problems and safeguards, appear likely to continue to defy resolution. New issues, such as trade in services, investment and intellectual property, are also likely to present serious difficulties for the negotiations.

Whether or not the Free Trade Agreement is implemented, Canada has a vital interest in the Uruguay Round and the strengthening of the GATT system. The Uruguay Round negotiations are not an alternative to the Canada-U.S. Free Trade Agreement; the two approaches are complementary. Failure to implement the FTA by Canada will reduce Canada's leverage in the GATT negotiations, while implementation of the Free Trade Agreement will strengthen Canada's multilateral negotiating position.

It is important to be realistic, however, about Canada's negotiating leverage, even with the Free Trade Agreement. If Canada is going to have some success in resolving agricultural trade problems and in achieving access objectives in offshore markets for upgraded resource products and high technology manufactured goods, Canada will need to continue to build coalitions such as the Cairns Group. Canada can play a helpful role in bridging the differences between developed and developing countries. Canada and the other middle-sized and small economies have the greatest stake in an open and more effective multilateral trading system, and thus, should be prepared to play an active and constructive role in the Uruguay Round.

Footnotes:

1. Murray G. Smith "What is at Stake?" in William Diebold (eds.) Bilateralism, Multilateralism and Canada in U.S. Trade Policy, (Cambridge, Mass. Ballinger for the Council on Foreign Relations, 1988.) See C. Michael Aho and Jonathan D. Aronson, Trade Talks: America Better Listen! (New York: Council on Foreign Relations, 1985 and 1987) and Gary Hufbauer and Jeffrey Schott, Trading for Growth: The Next Round of Trade Negotiations (Washington: Institute for International Economics, 1985).
2. United States Trade Representative, "U.S. Goals for Multilateral Trade Negotiations: Statement of the United States to GATT" September 7, 1985.
3. Institute for International Economics and Institute for Research on Public Policy, Reforming World Agricultural Trade; A Policy Statement by Twenty Nine Professionals, May 1988. See also William Miner and Dale Hathaway, (eds) World Agricultural Trade: Building a Consensus (Institute for International Economics and Institute for Research on Public Policy, 1988).
4. General Agreement on Tariffs and Trade, "Ministerial Declaration on the Uruguay Round" GATT 1396, 25 September 1986.
5. William Cline The Future of World Trade in Textiles and Apparel, (Washington, D.C.: Institute for International Economics, 1987), pp. 12-13, 165-169.
6. United Nations Commission on Trade and Development. "Developments in the Uruguay Round", May 4, 1988, page 43.
7. The Atlantic Council of the United States, The Uruguay Round of Multilateral Trade Negotiations Under GATT: Policy Proposals on Trade in Services, (Washington, D.C.: Atlantic Council, 1987).
8. F. Leutwiler et al. Trade Policies for a Better Future: Proposals for Action. (Geneva: GATT, 1985).
9. Richard Blackhurst, "Strengthening GATT Surveillance of Trade-Related Policies" in Meinhard Hilf and Ernst-Ulrich Petersmann (editors) The New GATT Round of Multilateral Trade Negotiations: Legal and Economic Aspects, (forthcoming, 1988).
10. See John H. Jackson, "The Birth of the GATT-MTN System: A Constitutional Appraisal," Journal of Law and Policy in International Business, vol. 12, no. 1 (1979), and John H. Jackson, "Government Disputes in International Trade Relations: A Proposal in the Context of GATT," Journal of World Trade Law, vol. 13, no. 1 (1979).

11. Gary Horlick, Geoffrey Oliver and Debra Steger, "Dispute Resolution Mechanisms" in Jeffrey Schott and Murray Smith (eds.) The Canada-United States Free Trade Agreement: The Global Impact (Washington and Ottawa: Institute for International Economics and Institute for Research on Public Policy, 1988).

DISCUSSION PAPERS SERIES

INSTITUTE DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS are issued from time to time by the International Economics Program of the Institute for Research on Public Policy.

The discussion papers series was inaugurated to disseminate nascent work on international economic topics sponsored by the Institute's International Economics Program. Papers are circulated to elicit constructive criticism and to stimulate discussion. This new series will complement the ESSAYS IN INTERNATIONAL ECONOMICS series of completed research monographs that is also sponsored by the International Economics Program.

Authors of discussion papers are completely free in developing each paper. Sponsorship by the Institute for Research on Public Policy implies neither approval nor disapproval of the ideas expressed.

Papers in the series include:

- 8501 "The World Economy 1984: Struggling after the Leader" by John M. Curtis*
- 8502 "Employment Dislocation Studies: An International Survey" by G.E. Salembier (July 1985)
- 8503 "Domestic Structural Adjustment Policies: A Comparative Survey" by G.E. Salembier (July 1985)
- 8504 "Negotiating Structural Adjustment Internationally: Challenges for National Trade Policy" by G.E. Salembier (July 1985)
- 8505 "Policy Research on Canada-United States Relations: Symposium Report" by Janis Doran (July 1985)
- 8506 "A Quantitative Assessment of the Costs and Benefits of the Footwear Import Quota" by A.R. Moroz and G.E. Salembier (June 1985)
- 8507 "Estimating Export Credit Subsidies" by A.R. Moroz (August 1985)
- 8508 "Approaches and Methodologies for Estimating Non-Tariff Barriers" by A.R. Moroz (August 1985)
- 8509 "Canada-United States Trade Relations: Bilateralism in a Multilateral Context" by John M. Curtis**
- 8510 "Economic Effects of Trade Liberalization with the USA: Evidence and Questions" by A.R. Moroz and Gregory J. Meredith (September 1985)
- 8511 "Trade Investment, and Knowledge in Relation to Multilateral Enterprises: The Canadian Experience" by D.C. MacCharles (December 1985)
- 8512 "World Grain Trade Financing: Past Patterns and Future Prospects" by David C. Cole and Susan Horton (December 1985)
- 8601 "Reflections on Canada-U.S. Relations in the Eighties" by Carl E. Beigie and John M. Curtis (January 1986)
- 8602 "Canada's Direct Investment in Western Europe" by Talaat Abdel-Malek (January 1986)

* No longer available. Published in Canada Among Nations 1984: A Time of Transition, edited by Brian W. Tomlin and Maureen Molot. (Toronto: James Lorimer, 1985), Chapter 5.

** No longer available. Published as "Bilateralism in a Multilateral World," International Perspectives (March/April 1985) 23-6.

- 8603 "Services and the General Agreement on Tariffs and Trade" by M.G. Clark (January 1986)
- 8604 "Institutional Provisions and Form of the Proposed Canada-United States Trade Agreement" by Frank Stone (April 1986)
- 8605 "Canada-Asean Relations: An Overview on Business Strategy and Government Policy" by Keith A.J. Hay and Donald Lecraw (August 1986)
- 8605A "Canada-Asean Relations: Indonesia" by Keith A.J. Hay and Donald Lecraw (August 1986)
- 8605B "Canada-Asean Relations: Thailand" by Keith A.J. Hay and Donald Lecraw (October 1986)
- 8605C "Canada-Asean Relations: Malaysia and Brunei" by Keith A.J. Hay and Donald Lecraw (November 1986)
- 8605D "Canada-Asean Relations: The Philippines" by Keith A.J. Hay and Donald Lecraw (December 1986)
- 8605E "Canada-Asean Relations: Singapore" by Keith A.J. Hay and Donald Lecraw (December 1986)
- 8606 "Strategic Management by Canadian Subsidiaries of U.S. Multinational Enterprises: Current Practices and Public Policy Implications" by Joseph R. D'Cruz (December 1986)

"Agricultural Trade and Trade Policy" a selection of papers (July 1986).

Services Sector Discussion Papers:

"The International Trade in Services Agenda - Origins, Evolution and Agenda" by Margaret L. Sims and Richard R. Rivers (January 1987)

"The Internationalization of Service Transactions: The Role of Foreign Direct Investment in International Trade in Services" by Brenda Siegel (January 1987)

"Trade in Services and the Experience of the European Economic Community" by Ivan Bernier (January 1987).

"The OECD Codes and Declarations and Trade in Services" by James A. Everard (February 1987)

"Federal-Provincial Jurisdictional Issues for Trade in Services Negotiations" by Mark Krasnick (1987)

Working Papers:*

Workshop on "Intellectual Property and International Trade: A Selection of Papers (November 1986)

-
- 8701 "An Annotated Inventory of Federal Business Subsidy Programs in the United States" by Anne A. Michel, Larry I. Good, Terry Bolger, Ellen Sweet, W. Martin Taylor and Andrew R. Moroz (May 1987)

-
- 8801 "Canada's Stake in the Uruguay Round and the GATT System" by Murray G. Smith (October 1988)
- 8802 "The Canada-United States Free Trade Agreement and the GATT" by Frank Stone (November 1988)

*Seminars on "Managed Trade Arrangements in Steel, Textiles and Clothing" (April 1986)

The Institute for Research on Public Policy

Founded in 1972, the Institute for Research on Public Policy is a national organization with offices in Victoria, Calgary, Toronto, Ottawa, London, Montreal, Quebec, and Halifax.

The raison d'être of the Institute is threefold: to act as a catalyst within the national community by helping to facilitate informed public debate on issues of major public interest; to stimulate participation by all segments of the national community in the process that leads to public policy making; to find practical solutions to important public policy problems, thus aiding in the development of sound public policies.

The Institute is now concentrating its core research program around three themes: International Issues, Governability, and Social Policy.

In addition, the Institute is continuing work in the Small and Medium-Sized Business Program and the Western Resources Program.

The Institute also undertakes a number of special research projects from time to time which do not fall under ongoing programs. Research findings are brought before the public through published books, reports, conferences and seminars, magazines and newspapers, and information briefs of government bodies.

International Economics Program

Murray Smith, Director (Ottawa)

As a part of the International Issues Theme, research on international economics is focussed on international and Canadian trade policy issues, and related monetary, investment and development issues. One main objective is to assess the impact of the changing world economic environment on smaller and medium-sized countries with open economies, such as Canada. The work of the program is aimed at making a contribution to the formulation and operation of policies in these areas, and stimulating public debate on the issues involved.